

REFINITIV STREETEVENTS

EDITED TRANSCRIPT

HSIC.OQ - Henry Schein Inc at Morgan Stanley Global Healthcare Conference

EVENT DATE/TIME: SEPTEMBER 05, 2024 / 3:30PM GMT

CORPORATE PARTICIPANTS

Stanley Bergman *Henry Schein Inc - Chairman and Chief Executive Officer*

Ronald South *Henry Schein Inc - Chief Financial Officer, Senior Vice President*

Tom Popeck *Henry Schein Inc - Chief Executive Officer - Healthcare Specialties Group*

CONFERENCE CALL PARTICIPANTS

Erin Wright *Morgan Stanley - Analyst*

PRESENTATION

Erin Wright - *Morgan Stanley - Analyst*

Okay. Good afternoon, everyone, and I'm Erin Wright, Healthcare Services at Morgan Stanley, and welcome to the Morgan Stanley Healthcare Conference. We're happy to have with us today a full lineup here from Henry Schein. So we have Stanley Bergman, Chairman and CEO; Ron South, SVP and CFO; as well as Tom Popeck, CEO of the Healthcare Specialty Group.

So with that, for some important disclosures before we get started, please see the Morgan Stanley research disclosure website at morganstanley.com/researchdisclosures. If you have any questions, please reach out to your Morgan Stanley sales representative.

And with that, I'll get started with the Q&A, if that's okay. So I guess, Stanley, I wanted to talk to you about sort of just how you think about sort of the underlying demand trends underlying health of the broader kind of dental market right now as you see it today?

QUESTIONS AND ANSWERS

Stanley Bergman - *Henry Schein Inc - Chairman and Chief Executive Officer*

Thank you, Erin, for hosting us. I lost my voice chasing grandchildren this weekend. So I'll try to speak as clearly as possible. The basic dental market is stable in North America. There are a couple of anomalies.

First of all, on the specialty side, the implant side, the high-end procedures are not as good, shall we say, from a demand point of view as they were a year, 1.5 years ago. I think it will come back, if interest rates come down a little bit. People are more positive about the economy. I think the same in the aligner field, although that's not a big part of our business. So generally, the market is good.

The equipment business is stable. If we take a look at where the equipment business was in 2019 and you draw a line -- it's been going quite well, but there was a lumpy period, 2020, '21, and we have the catch-up at the end of '21, '22. So I don't think it can take the business that Dentists were generating in '22 at the peak and draw a line from there, you have to take 2019 to go forward. And I think you'll see that it's basically quite stable.

Pricing has not increased this year from the manufacturers. It went up significantly in '22. There has been some price resistance, where manufacturers have adjusted. They continue to do, okay. But they haven't adjusted, business has gone to second-tier manufacturers and to own brand.

So the price increases of 2%, 3%, 4% that we saw a few years ago, we probably moved into the minus category. So I think this will settle out. This was an unusual anomaly.

Erin Wright - Morgan Stanley - Analyst

Okay. And then you did in the context of that lower guidance in the most recent quarter just on sort of a challenging backdrop from a macro perspective. And kind of slower than maybe you expected some of the recovery from the cyber incident as well. But what do you assume now, I guess, for the balance of the year, excluding some of the cyber incident dynamics? And how are you thinking about kind of those demand turns into 2025?

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

Yes. Well, Ron will give you statistics. But the cyber recovery has been going quite well. Each month, we do a little bit better, but it did not grow -- the gap did not decrease so we say or the sales in certain categories do not grow as fast as we expected. So it's somewhat of a delay, but we are closing that gap every month.

Ron, what guidance are we giving specifically?

Ronald South - Henry Schein Inc - Chief Financial Officer, Senior Vice President

Well, I think something we've pointed to, Erin, is that we do expect fourth quarter to be better than third quarter. And we have a number of things as we -- sequentially as we regain market share on the distribution side. That's part of it. Also, we did have the new implant launch right at the end of the second quarter as we begin to gain a little bit of momentum with that, that should contribute to some growth in the fourth quarter as well.

We also expect a little more normalization in our technology business in Henry Schein One coming out of some of the disruption that was caused by the Change Healthcare cyber incident that they had also some new technology products that are coming out that we think that will contribute to some revenue growth.

And then finally, we think bottom line will benefit a little bit better in the fourth quarter as we do initiate a new restructuring plan and some of the actions we're taking during the third quarter will provide a full quarter of benefit in the fourth quarter as well. So we do think as we move through the year, all those things are essential to us and executing on all those things are going to be essential for us to continue with the sequential growth that we're expecting.

Erin Wright - Morgan Stanley - Analyst

Okay. And then how are you thinking about just that promotional activity. We kind of talked about it in the most recent quarter and the nature of kind of some customers moving where there was more aggressive promotional activity, and it seems to be in very certain kind of categories that you're seeing this. Does that stabilize at some point in your view in terms of what you're seeing? And how much of it do you think is a function of that or math of the cyber intent -- or is it unrelated?

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

I think it's pretty stable. There are a couple of items like gloves where prices went up significantly, and so customers are looking at those prices. So there's a little bit of shopping over there. We disclosed that number. But generally, I think from a competitive point of view, things are stabilized.

And I think price adjustments that needed to be made by certain manufacturers, and it doesn't really impact our margin have been made. And I think that pricing is relatively stable, but at a lower number to where it was last year.

Erin Wright - Morgan Stanley - Analyst

Okay. And then share shifts, what are you seeing across the consumable space, has the dynamics there changed at all in terms of what you're seeing? I know you've had pretty stable kind of DSO relationships, but what about kind of below that in sort of that middle market or mid-tier kind of DSO?

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

I think with the larger DSOs, it's pretty stable. With the smaller ones, we are gaining some. I'm sure we were losing some. And generally, even with the smaller ones, we are closing that gap on business that we lost to the episodic buyers, I think it's relatively stable.

I think on the traditional side, traditional full-service distributors, I think we've come back, I don't think there's any erosion, maybe some of the websites for the episodic shift. But we own some of those websites, and we see that the movement is not significant.

Erin Wright - Morgan Stanley - Analyst

Okay. And then on dental equipment, I guess can you parse out kind of traditional versus high-tech equipment growth and demand trends, and you mentioned the higher interest rate environment. But any pockets where you're seeing kind of durability or areas where you're still seeing kind of pressure maybe CAD/CAM ASPs? Or has that stabilized and [you can think of that] category?

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

I think, traditional equipment. I think many made the mistake and looked at 2020 equipment took it from there. That was a bubble. If you ex out that bubble, the traditional equipment is pretty stable. It probably could be better if interest rates came down.

The CAD/CAM has so many dynamics. I think the mills for the first time we saw some stability last quarter, they are coming back. The IOS device, the scanners, there's a lot of dynamics there. We've gotten some imports coming in at a pretty low price. And I think if we see some innovation, which we're expecting to unfold in the not too distant future from some of our traditional brands, I think that will stabilize. But overall, we're predicting modest growth, but that was off some very good comps.

Erin Wright - Morgan Stanley - Analyst

Right. Great. And how do you think about relationships like for instance, your relationship with Dentsply? They recently announced this morning a new launch of a scanner prime scan too, how do you expect to kind of participate with that kind of offering, but also they're taking a hard look at some of their distributor relationships as well. I guess, how are your discussions and nature of those?

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

Yes. I mean, our relationship with Dentsply with Envista and with the spin-off of 3M, a little second-tier manufacturers is all pretty good. I don't think we have any issues that I'm aware of. It's helpful when our manufacturers come up with new products. We're very excited about the potential new product from Dentsply.

We hope to do well, it's around the world. And so I would say it's pretty good. We don't have any real issues. I mean, they would like us to sell more. We would like product at a lower price, but that's the nature of the game.

So I think our basic relationships are good, and we are first thing for new innovation, which the big players have not really introduced in a few years, but we're hopeful. Meanwhile, some of these new entrants have come in on some products, a little bit lower price, and they all have done quite well and we work with them all.

Erin Wright - Morgan Stanley - Analyst

And speaking of innovation and some areas of focus for you on specialty and the implant side. I guess can you talk about kind of -- well, let's take a step back and let's talk about recent demand trends in implants and kind of what you're seeing, whether it's premium or value and how would you characterize the current underlying environment in implants right now?

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

Currently. Right now, we have two sets of implant portfolios. One is focused on the high-end premium that we sell at a lower price, and then we have other brands like dentists and biotech and our business in Brazil, that is more of a discount brand. So we've been relatively well positioned. If you look at our business in Europe, particularly Germany, where we are, we believe we're the number one provider of implants, there's been no change in really new major products. So we've done very, very well.

In the US, we just introduced the new product. So our business was a bit frozen until the new product came. We thought we'd have at the beginning of the second quarter, we had it at the end of the second quarter. But overall, the premium side is doing okay. We don't really play heavily in the top end, but we have some business in that area.

And I'm looking at the top end of the procedures, and that's been impacted. And the more value products, we don't have a big portfolio, but the portfolio we have is doing relatively well. If you're only talking about implants, that's but maybe Tom is here, and he can talk about some of our other specialty businesses.

Erin Wright - Morgan Stanley - Analyst

Yes. No, that would be great. Yes, if you want to discuss kind of what's going on from an innovation standpoint across kind of specialty and your areas of focus, Tom, that would be great.

Tom Popeck - Henry Schein Inc - Chief Executive Officer - Healthcare Specialties Group

Sure. Well, some of the key focuses for us are endodontics -- orthodontics is a smaller part of our business, and a newer part of our business, which is orthopedics. In endodontics, we're the number two player. We've got a nice robust portfolio of new products that we're coming out with. Good growth this year.

Business is doing very well. On the orthopedic side, we expanded our orthopedic business, which was originally started with orthopedic cutting instruments and expanded that into extremity implants on the upper extremity handed wrist and foot and ankle.

My background is 11 years at Stryker. So I've been here at Henry Schein for five years, natural addition to our product portfolio, doing very well. Made those acquisitions earlier this year, and we're really encouraged with the progress we're making on the specialty products.

Erin Wright - Morgan Stanley - Analyst

That's great. And what percentage of kind of the total business is now what you focus on either from a revenue or EBIT perspective at this point?

Tom Popeck - Henry Schein Inc - Chief Executive Officer - Healthcare Specialties Group

I'm sorry, what?

Erin Wright - Morgan Stanley - Analyst

What percentage of, I guess, total Schein, I guess, do you look at from a specialty perspective, from a revenue or from an EBIT perspective, as I don't know, from --?

Ronald South - Henry Schein Inc - Chief Financial Officer, Senior Vice President

Well, I would say specialty business, specialty dental businesses, Tom's portfolio does not include implants. If you include implants in Tom's portfolio, it's about a \$1.2 billion run rate for us, right? If you tag on as well other kind of home solutions, for example, was that specialty, but we consider that more part of core medical, but things like Home Solutions within our medical business has greater growth and accretive margins versus that core medical business. So those other areas where we're investing as well that might not be necessarily seen as specialty businesses, but we do get better growth out of them.

Erin Wright - Morgan Stanley - Analyst

I guess that's what I was trying to get at in terms of the evolution of Henry Schein. And, Tom, you're here today to talk about some of the specialty businesses you look at, but there's also the dental specialty business and how that's evolved in terms of what is the mix of Henry Schein look like longer term in terms of how you're thinking about the mix of the business, where your areas of focus are and also just greater focus on some of those faster-growing inherently higher margin businesses like tech and specialty?

Tom Popeck - Henry Schein Inc - Chief Executive Officer - Healthcare Specialties Group

Yes. Well, if you take those dental specialty businesses and then add to it our technology business. Collectively, they are in the range of, say, 20% of our revenue at the most, probably more kind of closer to high teens, but we expect those businesses to contribute about 40% of our operating income by the end of the year. So it gives you a feel for the effect of those businesses. If you include other kind of company-owned brands that we sell, it increases that operating income mix to close to 50% of the total company.

So that's 50% of the operating income coming from brands that we own and we control.

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

And Tom is responsible for all of our own brands other than implants.

Erin Wright - Morgan Stanley - Analyst

Other than implants. Okay.

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

Well, he works closely with the implant people. On bone regeneration, that's part of the implant business, but his responsibility does include own new brands that are sold primarily to the distribution business, which is about 10% of our sales and quite profitable.

Erin Wright - Morgan Stanley - Analyst

And then in terms of going back to implants a little bit in the innovation there, could you talk a little bit about that being a driver for you as well as we kind of head into the second half, like you also did to an acquisition with the US FDA approval there. Just what are the initiatives? I guess, where do they stand now? And how meaningful can that be for Henry Schein?

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

Ron, what are we talking about in terms of what have we disclosed?

Ronald South - Henry Schein Inc - Chief Financial Officer, Senior Vice President

On implants, what we have said is that we do expect some growth in the back half of the year, largely driven by the Tapered Pro Conical launch of -- that BioHorizons had late in the second quarter. But also we're annualizing some of the acquisitions we did last year because we acquired Biotech in France effective April 1 of last year and SIN in Brazil effective July 1 of last year.

So we're going to be able to show -- and those are growing markets for us. So we do expect to talk about implant growth also on an internal basis for the back half of the year this year as well.

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

Because the Tapered Pro Conical has been in Europe for a while, and that's one of the reasons why we're doing so well in Germany with implants.

Erin Wright - Morgan Stanley - Analyst

Okay. Great, great. Yes. And as you think about also your orthodontic offerings, I should explain in the clear aligner offering, I guess, how do you expect that landscape playing out? You've kind of gone back and forth with Reveal. And then where does the strategy like from an orthodontic perspective?

Tom Popeck - Henry Schein Inc - Chief Executive Officer - Healthcare Specialties Group

Yes. So again, orthodontic business is small, right? But we have a recent acquisition with Biotech dental. They have an advanced product portfolio on the clear aligners. We're looking to transition to that.

We're in the midst of doing that, and really excited about what that could bring to us here in the US and globally.

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

But it's less than 10% of our specialty business.

Erin Wright - Morgan Stanley - Analyst

And then medical, I guess, can you remind us of kind of your unique positioning across kind of medical and the distribution market there are your key areas of focus and also kind of the competitive landscape, where it stands today. And just longer term, how do we think about growth across that medical segment?

Ronald South - Henry Schein Inc - Chief Financial Officer, Senior Vice President

Our medical business, as you're aware, is really confined to -- we don't serve the hospitals in the space that we really -- our strategy has always been to follow the patient. And as more and more procedures have moved to the ambulatory surgical centers as they have moved to physician offices, and now as more and more patients are being cared for at home, that's what we're starting to make more investment.

So we did a very important acquisition last year when we bought Shield Healthcare in the back half of the year. We were able to take that, combine it with Prism, which was a home solutions business we acquired a couple of years earlier, and we have kind of merged them into a singular business under a holdco. So we have common management, common infrastructure that we can now begin to scale a little more. So we'll continue to look for growth opportunities in the Home Solutions side within the medical business.

That's what we -- like I said, that is a faster growing subsegment of medical than what our core medical business had been doing. Having said that, core medical is still doing quite well. It gets a little lumpy because it frequently will move with how well we do with certain product categories such as point-of-care diagnostic kits. You see spikes in demand when flu infection rates go up and things like that. So you can't get a little bit of lumpiness in medical, but we do like the long-term trend.

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

And this lumpy stuff we show that separately. They hold all.

Erin Wright - Morgan Stanley - Analyst

Yes, that's helpful.

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

Number one. And number two is the profits have been pretty good, but there have been a number of injectables that have moved to generic form. That has brought down the price, but actually has done quite well with the profits.

Erin Wright - Morgan Stanley - Analyst

Got it. And in the home health market, how fast is that growing?

Ronald South - Henry Schein Inc - Chief Financial Officer, Senior Vice President

I wouldn't want to put an actual number on it, but I would say our expectations are that we can grow anywhere from mid- to high single digits in that area. I mean, while core medical was probably something closer the market -- long-term market growth that we expect on core medical would be more in that 4% to 7% range. I think this year, it's kind of trending more closer to the floor in terms of the market, but I would think Home Solutions are exceeding that 4% growth rate right now.

Erin Wright - Morgan Stanley - Analyst

Okay. And then tech and value-added services, a key kind of profit driver also across your business. I guess, how are you thinking about some of the dynamics going on with whether -- with this cyber incident dynamics with Henry Schein One, I guess, how it was influencing that, but also to that broader segment in terms of your tech and value-added services and how you think about near term as well as longer term, I guess, growth opportunities across the segment?

Ronald South - Henry Schein Inc - Chief Financial Officer, Senior Vice President

Well, the growth opportunities there are quite good. We look at it as even though we have a significant market share in practice management systems, there's still a very good opportunity for us in terms of share of wallet within our existing customers, as we have developed some additional kind of technological solutions for them, such as Detect AI, which has been a product that we are pretty excited about.

Detect AI allows a dentist to very efficiently and really kind of -- to diagnose cavities as well as carries that may not be necessarily visible to the naked eye. So this has been an area that has -- is gaining in popularity and it is sold as a subscription-based service through Henry Schein One.

So those are the types of products will be business analytics that we have been able to introduce that really give the practice is a very good kind of dashboard snapshot of how they're doing as a business.

Our DSO customers like it because it gives them an opportunity to benchmark some of their practices as well. So these are all areas where there's good opportunity for us to increase share of wallet beyond selling that practice management system where we have arguably about a 50% market share right now.

Stanley Bergman - Henry Schein Inc - Chairman and Chief Executive Officer

I think what is also important is the model is changing. We're moving to SaaS. So in the past, we've recognized the sale upfront. Now it moves to a monthly payment. So the sales may not look as good as they have historically, but the profits are good.

The units are there and more of the business is moving to the SaaS model.

Erin Wright - Morgan Stanley - Analyst

And then talking a little bit in the last few minutes here, capital deployment, I guess, M&A has been a key part of the strategy as well over the years. I guess, what does the pipeline look like? Where is the focus now, you mentioned home health. You've done several deals there. You're bringing Tom along as there are more along in that arena as well.

Yes, can you talk a little bit about the inorganic opportunities?

Ronald South - Henry Schein Inc - Chief Financial Officer, Senior Vice President

Certainly. So last year, we did approximately \$1 billion in acquisitions, which is by far the most we've ever done. This year has been a year that we really want to focus on integrating those acquisitions, but also continuing to be opportunistic in those areas, where we see opportunities for accelerated growth or higher margins. The best example is the Orthopedics business that Tom just described. We closed on that acquisition around April 1.

Another area that we are looking at and making some investments in this year, our acquisition strategy historically has included frequently acquiring a business where there is an owner-operator who stays in as a minority partner with us. After a number of years, we are then able to frequently, that owner operator wants to exit, we buy that owner-operator out.

So we have been a little more aggressive this year in investing in businesses where we already had a controlling interest, but now we're taking that interest to 100% because it does increase the leverage opportunities for us. We've done that in Tom's area in two of the businesses within endodontics, for example, that's going to give us some much greater opportunity to kind of bring some of the resources together within endodontics as one example.

There are a couple of other areas as well where we see great leverage opportunities once we don't have to kind of work with a minority partner in terms of the split of what's the appropriate split of profits on certain things and et cetera. So that's been an area of focus this year for us on the M&A side as well.

Stanley Bergman - *Henry Schein Inc - Chairman and Chief Executive Officer*

Of course, these minority partners were very important as we entered into particular areas. But the meanwhile, we've developed our own management capability in these specialty areas. The other area of investment has been our global e-commerce platform, which we've been investing in for the past three years. It went live in the UK in one of our businesses a few weeks ago.

It looks pretty good. So we've had expenses in this area, and we will have expenses, but the related sales will take time to come as these systems are installed or unfolded in different countries, but the system is up and running now in the UK.

Erin Wright - *Morgan Stanley - Analyst*

Okay. Great. And then as we think about sort of the broader dental market, there just does seem to be a large focus on just underlying demand trends. When will that turn? And like how thinking about -- you mentioned it's stable, but there are kind of pockets of isolated maybe pressure or like equipment dynamics, et cetera, at play.

But what are some other areas, I guess, that you think are the biggest underappreciated opportunities that you're seeing now across your business like outside of that may be disconnected from that underlying (inaudible)?

Stanley Bergman - *Henry Schein Inc - Chairman and Chief Executive Officer*

I think we have this particular anomaly of catching up from where we were before the cyber incident. The gap is narrowing. I think we'll work through that this year, probably a little bit into next year. But essentially, the market is stable. It's growing.

I think we'll see price increases coming back into play next year in the early part, not significant. But if you have two factors going on, one is the reduction in sales because of the cyber incident, which annualizes for us in the middle of October. And at the same time, you have no price increases, yet your costs go up because of inflation, which we're addressing through our restructuring, I think all of that results in incremental growth in EPS and certainly cash flow.

Erin Wright - *Morgan Stanley - Analyst*

Okay. All right. Well, thank you so much for the time. I really appreciate it. And yes, you have a great conference.

Stanley Bergman - *Henry Schein Inc - Chairman and Chief Executive Officer*

Thanks.

Ronald South - *Henry Schein Inc - Chief Financial Officer, Senior Vice President*

Thank you.

DISCLAIMER

Refinitiv reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES REFINITIV OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2024, Refinitiv. All Rights Reserved.